1-7-2009

Storey Const. Inc. v. Hanks Amicus Brief Dckt. 35459

In the Supreme Court of the State of Idaho

STOREY CONSTRUCTION INC.,	)	
	)	Supreme Court Docket No. 35459-2008
Plaintiff-Respondent,	)	
	)	Blaine County District Court DC
vs.	)	No. 2007-1043
	)	
TOM HANKS and RITA WILSON, husband and wife; and LILY REEVES,	)	Ref. No. 08-478
	)	
Defendants-Appellants.	)	
	)	

BRIEF OF THE IDAHO TRIAL LAWYERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF APPELLANTS

Appeal from the District Court of the Fifth Judicial District for Blaine County
Honorable Robert J. Elgee, District Judge Presiding

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I. IDENTITY AND INTEREST OF AMICUS CURIAE

The Idaho Trial Lawyers Association ("ITLA") respectfully submits this Brief as Amicus Curiae in accordance with the Court's Order dated December 11, 2008. ITLA is a voluntary, state-wide bar association with nearly 350 members, many of whom represent homeowners in construction disputes with builders. These members and their clients will be affected by the Court's ruling on whether a breach of contract claim arising out of a latent defect in a home is barred by the doctrine of res judicata where there has been a prior fee arbitration between the homeowner and builder. ITLA is concerned that the position advocated by Storey Construction Inc. ("Storey Construction") and adopted by the District Court will deny ordinary homeowners important remedies and shift the economic burden of poor construction to those who can least afford it. For those reasons, ITLA urges the Court to reverse the District Court's decision and remand this case to the District Court with instructions to compel an arbitration.

II. ARGUMENT

A. Standard of Review.

The District Court ruled that Tom Hanks and his wife, Rita Wilson, (collectively referred to as "Hanks") cannot arbitrate a claim for latent construction defects in their home because their claim was barred by the doctrine of res judicata after they arbitrated a fee dispute with Storey Construction. The issue of whether a claim is barred by res judicata is a legal question upon which this Court exercises de novo review. Waller v. State, 146 Idaho 234, 192 P.3d 1058, 1061 (2008).

B. The District Court's Application of Res Judicata is Not Consistent with Idaho Law.

The issue to be decided by the Court is whether the District Court erred when it ruled that the doctrine of res judicata barred Hanks' claim for latent construction defects. Res judicata is a judicial doctrine with roots in the Latin phrase "Res judicata pro veritate accipitur" or "a matter adjudged is taken for truth." Barbara Anderson Gimbel, The Res Judicata Doctrine Under Illinois and Federal Law, 88 Ill. B.J. 404 (July 2000). In 1983, the Court adopted the Restatement (Second) of Judgments' formulation of res judicata. Aldape v. Akins, 105 Idaho 254, 259, 668 P.2d 130, 135 (1983) (hereinafter referred to as "Restatement"). The general rule under the Restatement is: "A valid and final personal judgment rendered in favor of the defendant bars another action by the plaintiff on the same claim." Restatement (Second) of Judgments § 19 (1982) (emphasis added).

When the term "claim" is used in the Restatement it means " . . . all rights of the plaintiff to remedies against the defendant with respect to all or any part of the transaction, or series of connected transactions, out of which the action arose." Restatement (Second) of Judgments § 24(1) (1982). Determining what constitutes a "transaction" is to be a "pragmatic" endeavor:

> **What factual grouping constitutes a "transaction", and what groupings constitute a "series" are to be determined pragmatically**, giving weight to such consideration as whether the facts are related in time, space, origin, or motivation, whether they form a convenient trial unit, and whether their treatment as a unit conforms to the partie

Id. at § 24(2) (emphasis added). The purpose of res judicata is to: (1) avoid inconsistent results in multiple suits; (2) protect the courts against repetitious litigation; and (3) protect litigants from

vexatious litigation. Adalpe, 105 Idaho at 257, 668 P.3d at 133 (citations omitted).

In 2007, Hanks initiated a claim against Storey Construction for latent construction defects in their home and other outbuildings on their property by making a demand for arbitration. Storey Construction declined to arbitrate and filed a Complaint against Hanks in the District Court alleging abuse of process. The essence of Storey Construction's argument was that the parties had previously arbitrated their disputes and the award in that case extinguished all of Hanks' claims, including any claim for latent defects that could not have been known at the time of the first arbitration. The District Court held a "summary trial" on the res judicata issue and ruled in Storey Construction's favor.

Storey Construction advocated, and the District Court adopted, the view that there was only one transaction between Storey Construction and Hanks – the contract for construction. Under this view, all claims arising out of the contract had to be raised and decided during the first arbitration or they were forever barred. The Court ruled:

> I think this current claim made by defendants is the same claim under the res judicata analysis that's made in the first arbitration. **It's based on the operative set of facts of construction of the buildings and that operative set of facts ended when the construction ended. The damages were felt at different times and under different circumstances, but to me that doesn't affect the application of the res judicata.**

(6/19/08 Tr., p. 98, lines 13-20). The District Court's analysis was contrary to the Restatement's "pragmatic" criteria set forth in § 24(2).

To begin with, it is apparent from the District Court's analysis that it only looked at the origin of Hanks' claim. The court reasoned that since the claim for latent defects arose out of the same construction contract that was previously arbitrated, it was barred. Origin, however, is only one factor that is to be considered when deciding whether to apply res judicata.

The District Court's analysis is also contrary to the parties' written agreement (i.e., their expectations) and common construction industry usage and understanding. When Storey Construction and Hanks entered into an agreement for the construction of Hanks' home, they also agreed to a set of General Conditions that were applicable to their relationship. See Exhibit 1 (A) (Construction Agreement between SVT and Storey). The General Conditions are an excellent indicator of common usage and understanding in the construction industry because they are a standard, American Institute of Architects form document.[1] They are also an excellent indicator of Storey Construction and Hanks' expectations because it is apparent on the face of the document that the parties negotiated extensive changes (revisions are shown) and indicated their agreement by initialing each page. This is not a case where boilerplate was simply incorporated by reference.

Article 4.3 of the General Conditions governs claims and disputes between the parties. Distilled to its essential parts, Article 4.3 provides that the parties will arbitrate any "Claim" arising

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[1] AIA form contracts are commonly used because they are relatively inexpensive and have been litigated extensively throughout the United States. The AIA claims that its contract documents "have defined the contractual relationships in the design and construction industry for 120 years." See www.aia.org/docs.

out of or related to the Contract. See 4.6.1. The term "Claim" is defined as:

> . . . a demand or assertion by one of the parties seeking, as a matter of right, adjustment or interpretation of Contract terms, payment of money, extension of time or other relief with respect to the terms of the Contract. The term "Claim" also includes other dispute between the Owner and Contractor arising out of or relating to the Contract. Claims must be initiated by written notice. The responsibility to substantiate Claims shall rest with the party making the claim.

See 4.3.1 of General Conditions.

While "claim" is defined broadly, there is an important limitation that the District Court did not consider when it made its decision. Section 4.6.5 of the General Conditions states: "The party filing a notice of demand for arbitration must assert in the demand all Claims **then known to that party** on which arbitration is permitted to be demanded." (Emphasis added). In other words, if the parties know about a claim they have to raise it. If they do not know about a claim, then they do not have a duty to raise it. In fact, it would be impossible to raise an unknown claim.

The construction defects at issue now were not at issue at the time of the parties' first arbitration. This is apparent because Storey Construction is not making a collateral estoppel argument and because the District Court expressly ruled that the defects were "latent" at the time of the original arbitration for purposes of deciding the res judicata issue. (6/19/08 Tr., p. 90, line 11 - p. 91, line 14). A latent defect is "[o]ne which could not be discovered by reasonable and customary observation or inspection." BLACK'S LAW DICTIONARY 883 (6th ed. 1990). If the defects at issue could not have been known by Hanks at the time of the first arbitration, then they had no obligation

to raise them under the parties' agreement.

The District Court made much of the fact that Hanks alleged in a counterclaim in the first arbitration the existence of substandard work. (6/19/08 Tr., p. 94, line 14 - p. 95, line1). The fact that Hanks did not actually offer any evidence on the claim was irrelevant to the District Court's ruling. Id. The Court likened the situation to a typical car wreck where a plaintiff has to bring "everything you know to bear" when making a claim and cannot make a second claim for later discovered damages. (6/19/08 Tr., p. 93, lines 11-24). The District Court's analogy misses the mark.

A construction contract does not involve a single, isolated event like a car wreck. A construction contract involves literally countless "transactions" and the parties to it have rights and obligations that exist even after a project is completed. The number of transactions and ongoing rights and obligations make the claims process in a construction case much different than an ordinary car wreck. A hypothetical situation demonstrates this point.

Assume that a school district employs a builder to add a new wing to a high school. During the course of construction, a dispute arises between the builder and one of its subcontractors which results in a lien being placed against the school district's property. The school district, following the same standard, AIA General Terms and Conditions at issue in this case, makes a demand for arbitration against the builder. In that demand the school district, which is obligated to assert all known claims, also alleges "substandard work" (its claim is made in accordance with traditional

notice pleading requirements) and presents evidence at the arbitration that the windows on the project were installed incorrectly. The arbitrators subsequently enter a decision in favor of the school district which is then reduced to a judgment.

Three years after the first arbitration decision the school district discovers that the roof is failing due to substandard workmanship. Specifically, a vapor barrier is missing in parts of the building and has been missing since the roof was completed. There is an express warranty in the parties' contract that the roof will last for ten years from the date of completion of the project.

Under the District Court's analysis, the school district's claim for the missing vapor barrier would be barred by the school district's mere allegation of substandard workmanship at the time of the first arbitration. The fact that the missing vapor barrier was not at issue in the first arbitration and was unknown to the school district is irrelevant. The fact that the missing vapor barrier has no connection whatsoever to the defectively installed windows is irrelevant. The unfortunate and unforeseen result of the District Court's ruling would be the nullification of an express warranty that was supposed to protect the school district for ten years. This is an unjust result and one that is not warranted under Idaho's res judicata law.

The District Court's ruling is an improper extension of Idaho's res judicata law and jeopardizes the remedies to which Idaho's homeowners are entitled. This is not a case where Hanks is taking a "second bite at the apple." There is no evidence in the record that shows the latent defects at issue were connected in any way to the claims that were litigated in the first arbitration. The only

way the District Court was able to conclude that the claim should be barred is simply because it arose out of the same construction contract. That is not the standard for res judicata under Idaho law. Because the District Court erred as a matter of law, this Court should reverse the decision and remand this case with directions to compel an arbitration.

C. This Court Has Long Recognized as a Matter of Public Policy that Builders are in the Best Position to Prevent Latent Defects.

Over the years, the Court has carved out a number of exception to Idaho's res judicata laws. For example:

* Heaney v. Bd. of Trustees of Garden Valley School Dist. No. 71, 98 Idaho 900, 575 P.2d 498 (1978) (holding that superintendent's failure to join claim for damages with action for writ of mandamus did not preclude him from later bringing a damages claim).

* Duthie v. Lewiston Gun Club, 104 Idaho 751, 663 P.2d 287 (1983) (holding that second claim was not barred because it was not ripe at the time of the first adjudication).

* Nash v. Olverholser, 114 Idaho 461, 757 P.2d 1180 (1988) (holding that tort action against spouse for assault and battery was not barred even though it could have been brought in divorce action).

While ITLA does not believe that the Court has to make any public policy "exception" in order to reverse the District Court's decision, there is certainly ample grounds for doing so.

The Court has long recognized that public policy considerations in latent construction defect cases warrant special consideration. See e.g., Tusch Enterprises v. Coffin, 113 Idaho 37, 740 P.2d 1022 (1987). In Tusch, the Court made two important holdings. First, it held that an implied warranty of habitability does not apply just to consumers who live in a home – it also applies to

sophisticated buyers who have purchased the property to make money. 113 Idaho 47, 740 P.2d at 1032. Second, the the subsequent purchaser of a residential dwelling can assert a claim for breach of the implied warranty of habitability even though there is no privity of contract with the builder. 113 Idaho at 50-51, 740 P.2d at 1025-26. Both of these holdings represent a substantial departure from Idaho contract law, but the Court felt it was warranted. The Court explained its decisions as follows:

> [B]y virtue of superior knowledge, skill, and experience in the construction of houses, a builder-vendor is generally better positioned than the purchaser to know whether a house is suitable for habitation. He also is better positioned to evaluate and guard against the financial risk posed by a latent defect, and to absorb and spread across the market of home purchasers the loss therefrom. In terms of risk distribution analysis, he is the preferred or 'least cost' risk bearer. Finally, he is in a superior position to develop or utilize technology to prevent such defects; and as one commentator has noted, 'the major pockets of strict liability in the law' derived from 'cases where the potential victims . . . are not in a good position to make adjustments that might in the long run reduce or eliminate the risk.'

Tusch, 113 Idaho at 47-48, 740 P.2d at 1032-33 (citations omitted).

These same public policy considerations should apply when deciding whether to apply res judicata to a latent construction defect case. Admittedly, Hanks and his wife are not ordinary Idaho consumers, but the rule of law adopted by the Court will have an impact on Idaho's less prominent and less resourceful citizens for years to come. If a claim for a construction defect is truly latent (as the District Court assumed in this case) and the issue of that particular defect has not previously been litigated by the parties, the Court should allow the parties to adjudicate their dispute whether it be

in an arbitration setting or in the courts. There is no risk of inconsistent judgments (one of the stated purposes of res judicata) and there is no harm to the courts or an arbitration tribunal in adjudicating a claim on its merits. The biggest risk is to the builder who may have to deal with multiple claims. The builder, however, is the one who was in the best position to avoid the multiple claims in the first place. Storey Construction argued that there would be countless lawsuits arising out of the same construction contract if Hanks' position were to be adopted. The argument is overstated. Builders and homeowners have the same motivation in construction disputes – get the dispute resolved as quickly and efficiently as possible. Homeowners are not motivated to bring piecemeal litigation because construction litigation is expensive and protracted. If a homeowner is truly engaging in vexatious litigation (i.e., is only bringing claims to harass the builder), there are remedies that can be employed to deter that behavior. Sanctions can be ordered or a claim for abuse of process can be made. The possibility of vexatious litigation does not outweigh the Court's articulated public policy considerations. Because public policy favors the adjudication of disputes involving latent construction defects on their merits, the District Court's ruling should be reversed and this case should be remanded with direction to compel an arbitration.

D. The District Court's Analysis of Waterfront Misses the Mark.

The District Court commented during oral argument that it felt compelled to follow the Virginia Supreme Court's decision in Waterfront Marine Construction, Inc. v. North End 49ers Sandbridge Bulkhead Groups A, B and C, 468 S.E.2d 894 (1996). (6/19/08 Tr., p. 98, line 21 - p.

99, line 1). Implicit in the District Court's ruling is the notion that the Waterfront case somehow justified the court's decision to apply res judicata to the facts of this case. The District Court's analysis of the Waterfront decision misses the mark.

In the Waterfront case, a group of landowners in Virginia contracted with a construction company to build a "bulkhead" between their properties and the beach. During the course of construction, the landowners had an expert inspect the bulkhead after a similar bulkhead failed; the inspector found that the bulkhead was defective. Id. at 896. The landowners demanded arbitration and sought damages to correct the work. Id. The builder responded with its own arbitration demand for the unpaid balance of the construction price. Id.

The arbitration panel denied the landowners' claim for money damages, but did order that the builder do certain work related to tie rod connections and anchor piles. Id. The work was to be done to the satisfaction of an independent engineer and had to be guaranteed for a period of one year after completion. Id. at 896-97. The work was to be done within 60 days of the arbitration panel's decision. Id. The parties could not agree on an independent engineer and so the builder never completed the work. Id. Approximately 8 months after the arbitration panel issued its decision, a series of storms hit the coast. The bulkhead was seriously damaged. Id.

After the bulkhead was damaged, the landowners made another demand for arbitration based on the builder's breach of warranty. The request was granted and the construction company appealed. The Virginia Supreme Court ruled that res judicata barred the landowners' demand. 468

S.E.2d at 904-05.

The ruling in Waterfront, while unfortunate for the landowners, is consistent with res judicata principles. The landowners knew the bulkhead was defective. They brought a claim against the builder for those defects. The arbitrators ruled against them. The storms proved that the arbitrators were wrong. Juries and courts sometimes make the wrong decision. Nonetheless, the law provides that a claimant does not get to relitigate the same issue simply by attaching a new label to the claim.

The District Court did not recognize that the situation in Waterfront is substantially different than the situation in this case. Hanks did not know about the latent defects at the time of the first arbitration. There is no way that the latent defects could possibly have been raised or adjudicated. There is no evidence that the latent defects were in anyway related to what was adjudicated during the first arbitration. The only possible connection is that they arose out of the same construction contract. That does not meet the requirements for the application of res judicata.

The bottom line is that the District Court's conclusion that the Waterfront decision justified its decision to bar Hanks' claim is error. The Waterfront case is distinctly different from the facts of this case and has no application except to demonstrate that Hanks' claim should not be barred by res judicata. Because the District Court erred when it concluded that Hanks' claim was barred, the decision should be reversed and this case remanded with directions to the District Court to compel an arbitration.

III. CONCLUSION

For the foregoing reasons the Idaho Trial Lawyers Association as Amicus Curiae urges this Court to reverse the District Court's ruling and remand this case with instruction to enter an order compelling Storey Construction to arbitrate Hanks' claim.

DATED this 7th day of January, 2009.

HEPWORTH, JANIS & BRODY, CHTD.

By: _____
Robyn M. Brody
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CERTIFICATE OF SERVICE

Robyn M. Brody, a resident attorney of the State of Idaho, hereby certifies that on the 7th day of January, 2009, she served a true and correct copy of the within and foregoing document upon the following:

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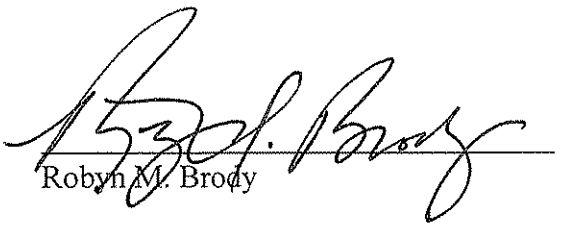

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